



Domestic Transfer Pricing

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Introduction to Transfer Pricing



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What is Transfer Pricing?



OECD Guidelines defines “Transfer Prices” as “the prices at which an enterprise transfers physical goods and intangibles or provide services to associated enterprises”

Thus, Transfer Pricing is a term used to refer to all inter company pricing arrangements between related enterprises

Transfer Pricing provisions were introduced to prevent shifting of profits by MNCs from high tax rate jurisdiction to low tax rate jurisdictions to minimize tax cost at group level

Evolution of Transfer Pricing

| Year | Events occurred |
|---------------|---|
| 1991 | Integration of Indian economy with Global economy leading to increased cross border transactions |
| March 1999 | The Standing committee on Finance realized that existing tax provisions (Section 92) may not be effective to curb Transfer Pricing abuse in India |
| November 1999 | CBDT constitutes an Expert Group on Transfer Pricing for suggesting necessary amendments in the Act and regulatory Framework |
| January 2001 | Expert Group submitted its report to CBDT |
| February 2001 | Finance Ministry introduces Chapter X to deal with transfer pricing issue with effect from AY 2002-03 (ie FY 2001-02) |

TRANSFER PRICING REGULATIONS IN INDIA

- Any international transaction undertaken between associated enterprises would be subject to transfer pricing regulations and the transfer price charged/paid should be at arm's length
- The term "international transaction" is widely defined to cover almost all kinds of transactions
- Associated Enterprise is also defined to cover **direct or indirect** shareholding of more than 26% or various other criteria by way of participation in the management or control
- Indian Transfer Pricing regulations are based on OECD Guidelines but with some modifications

TRANSFER PRICING COMPLIANCES & PENALTIES ON DEFAULT



| Sections | Provisions | Applicability of Specified Domestic Transactions |
|----------|---|--|
| 92 | Computation of Income having regard to Arm's Length Price | Yes |
| 92A | Meaning of Associated Enterprise | No |
| 92B | Meaning of International Transaction | No |
| 92C | Methods of Computation of Arm's Length Price | Yes |
| 92CA | Reference to Transfer Pricing Officer | Yes |
| 92CB | Safe Harbour Rules | Yes |
| 92CC | Advance Pricing Agreement | No |
| 92CD | Effect of Advance Pricing Agreement | No |
| 92D | Maintenance of Information and Documents | Yes |
| 92E | Accountant's Report | Yes |

APPLICABILITY OF TRANSFER PRICING

Section 92B International Transaction

- purchase, sale, transfer, lease or use of tangible as well as Intangible property
- capital financing, including borrowings, lending, guarantees, deferred payments, etc arising during the course of business
- provision of services
- transaction of business restructuring or reorganization, irrespective of whether it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date

ASSOCIATED ENTERPRISE

- Which participated directly or indirectly, or through one or more intermediaries in Management or Control or Capital of the Other Enterprise
- In respect of which one or more persons participate directly or indirectly or through one or more intermediaries in Management or Control or Capital of two enterprises

Associated Enterprise also include Deemed Associated Enterprises like:

- one enterprise has direct or indirect shareholding carrying not less than 26% voting power in the other enterprise
- one person holds 26% or more of the voting power in two enterprises
- Others

Arm's Length Price

Arm's length price means a price applied or proposed to be applied in a transaction between non Associated Enterprises in uncontrolled conditions

• Arm's length price can be determined by any of the following methods:

- Comparable Uncontrolled Price Method
- Resale Price Method
- Cost Plus Method
- Profit Split Method
- Transactional Net Margin Method
- Other Method as prescribed under Rule 10AB

Arm's Length Price

- Where arm's length price is within 5% range of the transaction price, no adjustment is warranted but if it is beyond 5% range, adjustment is required to be made to the transfer price and benefit of 5% is not available (5% range is applicable for A.Y.2012-13). For A.Y.2013-14 onwards, tolerance range would be notified by the central government subject to maximum 3%



INTRODUCTION TO DOMESTIC TRANSFER PRICING



GLAXO SMITHKLINE CASE

Decision of the H'ble Supreme Court in the case of Glaxo Smithkline Asia (P) Ltd [236 CTR 113]

The H'ble Supreme Court while deciding on the issue of section 40A(2) made some of the important observations as under:

- ❖ The present Transfer Pricing Regulations does not apply to domestic transactions
- ❖ In domestic transactions, under-invoicing and over-invoicing will be revenue neutral, except in two circumstances:
 - i. where one of the related entities is loss making or
 - ii. where one of the related entities is liable to pay tax at a lower rate and the profits are shifted to such entity
- ❖ The question of extending Transfer Pricing regulations to domestic transactions require expeditious consideration by the tax authorities

GLAXO SMITHKLINE CASE

- The CBDT should examine whether Transfer Pricing Regulations be extended to domestic transactions by making amendments to the Act
- Law can be amended to mandate the taxpayer to comply with Rule 10D
- Assessing Officer can be empowered to make adjustments to value of the transactions between the related parties based on methods of determination of arm's length price

Based on the above observations of the H'ble Supreme Court, the Finance Act, 2012 has extended the applicability of the transfer pricing provisions for specified domestic related party transactions

PURPOSE OF INTRODUCING DOMESTIC TRANSFER PRICING

It was realized by the government that:

- ❖ Presently, there is no method prescribed to determine reasonableness of expenditure to re-compute the income in related party transactions
- ❖ There is need to provide **objectivity in determination of income** and determination of reasonableness of expenditure in domestic related party transactions
- ❖ There is need to create **legally enforceable obligation** on assessee to maintain proper documentation

INTRODUCTION – FINANCE ACT 2012

- ❖ Based on the above observations of the H'ble Supreme Court, the Finance Act, 2012 has extended the applicability of the transfer pricing provisions for specified domestic related party transactions
- ❖ Seeks to create legally enforceable obligation on taxpayers to maintain proper documentation
- ❖ Is intended to provide objectivity in determining reasonableness of expenditure and income eligible for tax holiday



Section 92BA

“Specified Domestic Transaction” means any transaction, **not being an international transaction**, namely:—

- i. any expenditure for which payment is to a person referred to in s.40A(2)(b);
- ii. any transaction referred to in s. 80A;
- iii. any transfer of goods or services referred to in s. 80-IA(8);
- iv. any business transacted between the assessee and other person under s. 80-IA(10);
- v. any transaction, under Chapter VI-A or s.10AA, if s. 80-IA(8) or s.80-IA(10) is applicable; or
- vi. any other transaction as may be prescribed,

and the aggregate of such transactions entered into in the previous year exceeds INR 5 Crores

The limit of 5 crore is increased to 20 Crore w.e.f. Assessment Year 2016-17



Earlier Methodology

Expenditures and Profit Linked Deductions

| Particulars | Nature | Transactions with | Earlier methodology |
|--------------|-----------------------|--|--|
| 40A(2) | Expenditure | Related parties defined | Excessive or unreasonable expenditure disallowed |
| 80A, 80IA(8) | Income or expenditure | Between different business units of same tax payer | Fair Market Value |
| 801A(10) | Profits | Close connection | More than ordinary profits |

including SEZs

SDT is triggered if the aggregate of the above mentioned transactions exceeds Rs. 5 crore during a financial year...

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ALP linked computation – S. 92(2A)



“Any allowance for an expenditure or interest or allocation of any cost or expense or any income in relation to the SDT shall be computed having regard to the arm's length price”

- ❑ In relation to Specified Domestic Transaction (SDT), the provision covers:
 - Allowance for an expense or interest
 - Allocation of cost or expense
 - Any income
- ❑ Cost contribution arrangements also covered [s.92(2)]
- ❑ The Chapter permits adjustment to income favorable to the revenue on item to item basis
- ❑ The Chapter neither permit downward adjustment nor set-off of one item against another nor corresponding adjustment in hands of other party
- ❑ Allocation of cost or expense is not SDT in itself

SPECIFIED DOMESTIC TRANSACTIONS

Section 40A

- Expenditure paid or to be paid to related party as defined under section 40A(2)(b)

Section 80IA

- Inter unit transfer of goods and services as referred to in section 80IA(8)

Some examples of Specified Domestic Transactions

- Transaction between the tax payer and any other person owing to close connection as referred to in section 80IA(10) where more than ordinary profits are earned by business unit claiming tax holiday/deduction

SPECIFIED DOMESTIC TRANSACTIONS

Section 10AA

- Any transaction under Chapter VIA or Section 10AA to which the provisions of 80IA apply, i.e.:
 - inter-unit transfers
 - more than ordinary profits earned by tax holiday/exemption unit

SPECIFIED DOMESTIC TRANSACTIONS – COMMON TRANSACTIONS

- 
- Payment for purchase of semi-finished goods
 - Transfer of machinery, technology, etc
 - Sharing of common costs
 - Job work charges
 - Payment of interest /royalty charges
 - Transfer of goods from one unit to another (in specific cases)
 - Payment made to key personnel/relatives
 - Rent charged

THRESHOLD LIMIT & COVERAGE

Domestic Transfer Pricing is applicable only where value of Specified Domestic Transactions crosses 5 Crs

- While computing the aggregate value of transactions:
 - Value of the International transactions to be excluded
 - Value of transactions between 2 units of the same company to be covered (when undertaken with a tax holiday unit)
- Inter-company transactions to be covered (when undertaken with a company having a tax holiday unit)
 - Transactions with a person having a close connection as mentioned in section 80IA(10) to be covered
 - Payment of expenses to related person defined under section 40A(2)(b) to be covered

THRESHOLD LIMIT & COVERAGE



Aggregate Value of transaction below INR 5 Cr

Subject to existing Tax laws

Aggregate Value of SDT above INR 5 Cr

Subject to Domestic Transfer Pricing regulations



DOMESTIC TRANSFER PRICING SECTION 40A(2)(b), 80IA(8) & 80IA(10) RELATIONSHIPS, ISSUES & CHALLENGES





Section 40A(2)

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Type of person covered in Section 40A(2)(b)

| Type of person | When covered |
|---------------------|--|
| Investor company | <ul style="list-style-type: none">Any company (say Company A) which has substantial interest* in Company B |
| Sister company | <ul style="list-style-type: none">Any company in which Company A has substantial interest (i.e. Company C) |
| Investee company | <ul style="list-style-type: none">Any company in which Company B has substantial interest (i.e. Company D) |
| Group company | <ul style="list-style-type: none">Any company of which a director has substantial interest in Company BAny company in which a director of Company B has substantial interestAny relative of such directors |
| Certain individuals | <ul style="list-style-type: none">Any director of Company BAny director of Company AAny individual who has substantial interest in Company BAny relative of the above individuals |

* Substantial interest is defined to include a 'beneficial owner of shares' carrying not less than 20% of voting power.

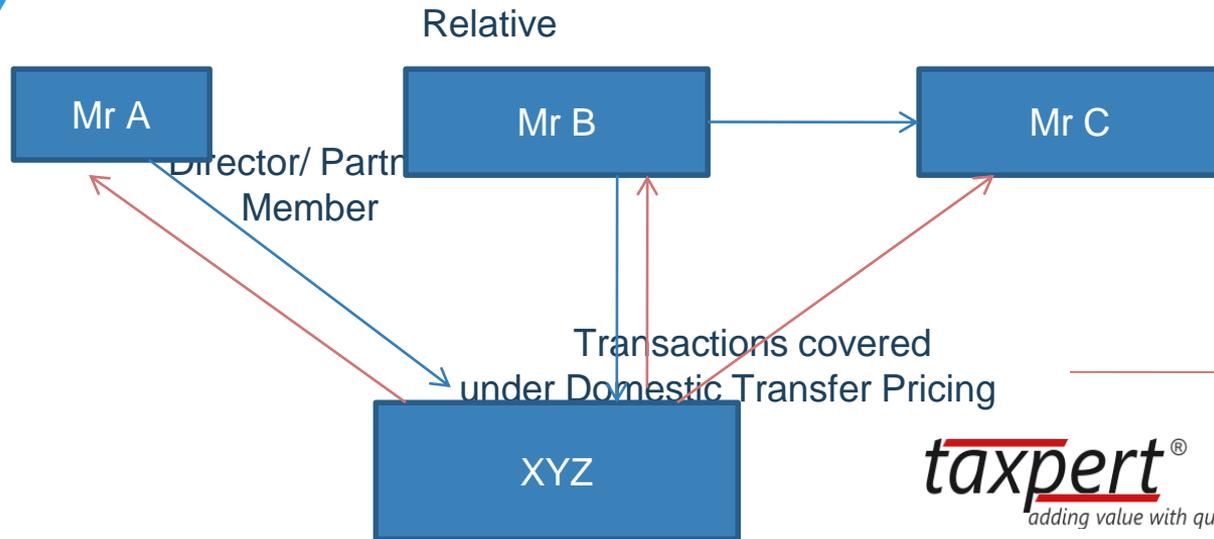
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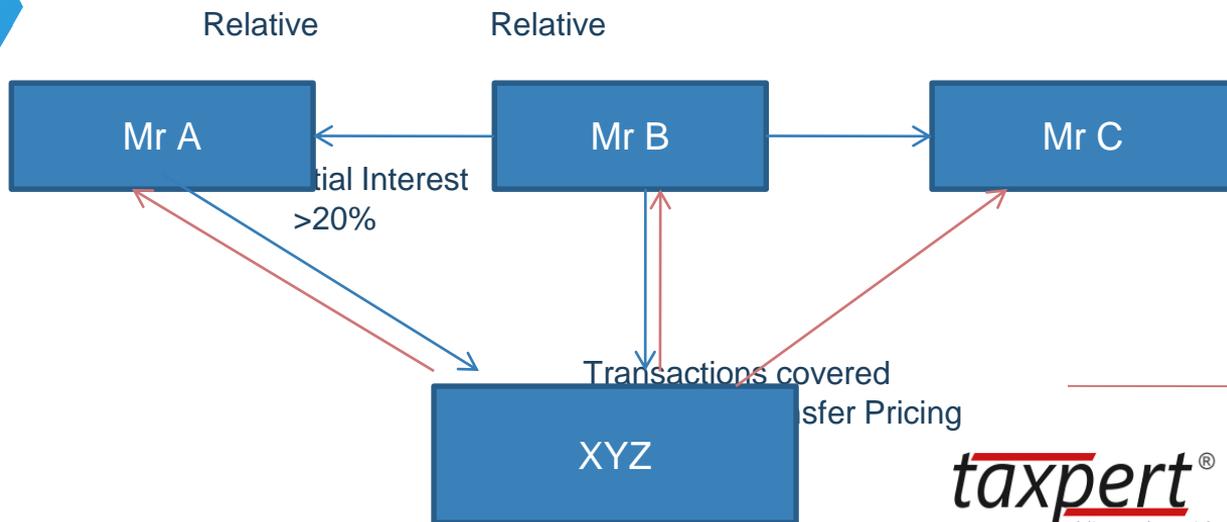
TRANSACTIONS COVERED

Case-I: Director or any relative of Director – Section 40A(2)(b)(ii)
Relative: in relation to an individual, means the husband, wife, brother or sister or any lineal ascendant or descendant of that individual



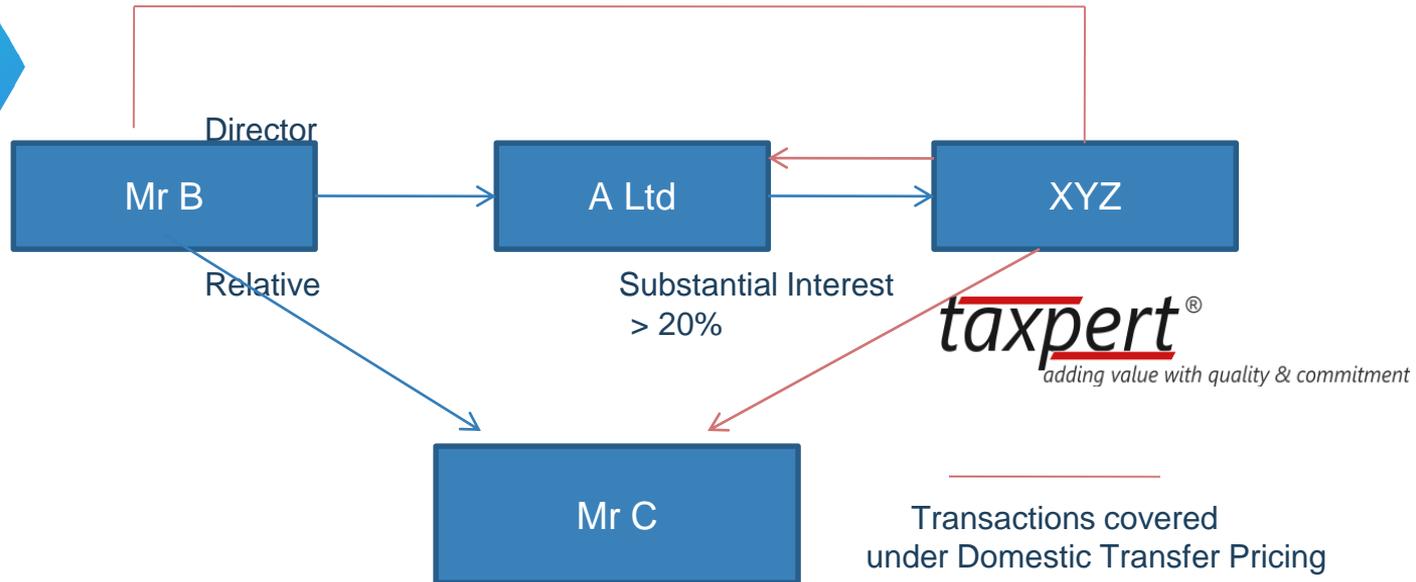
TRANSACTIONS COVERED

Case-II: To an individual who has substantial interest in the business of XYZ Ltd or relative of such individual – Section 40A(2)(b)(iii)
* Substantial Interest: The Beneficial owner of shares carrying not less than 20% of the voting power in the company



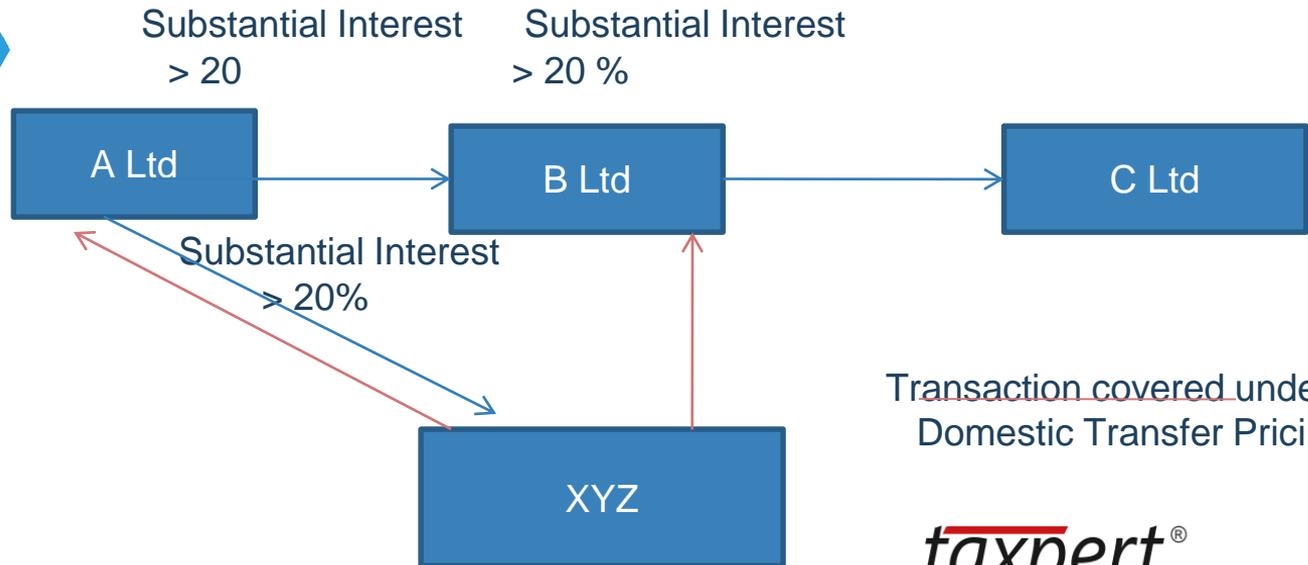
TRANSACTIONS COVERED

Case-III: To a Company having substantial interest in the business of XYZ Ltd or Director of such company or any relative of Director – Section 40A(2)(b)(iv)



TRANSACTIONS COVERED

Case-IV: Any other Company carrying on business in which the first mentioned company has substantial interest – Section 40A(2)(b)(iv)



TRANSACTIONS COVERED

Few more instances:

Case V : To a Company of which a director has substantial interest in the business of XYZ Ltd or any other director of such company or relative of director - Section 40A(2)(b)(v)

Case-VI: To a Company in which XYZ Ltd has substantial interest in the business of the company - Section 40A(2)(b)(vi)

Case-VII: Any director or relative of a director of XYZ Ltd having substantial interest in that person - Section 40A(2)(b)(vi)

40A(2) ISSUES AND CHALLENGES

- Benchmarking of Managerial remuneration?
- • Whether indirect shareholding is covered?
- • Whether Capital expenditure or corresponding depreciation is covered?
- • Whether shareholding of individual Directors can be aggregated for determining substantial interest?
- • Corresponding credit for tax neutral entities

40A(2) ISSUES AND CHALLENGES

- ❖ Section 40A(2)(b) includes remuneration paid to the management.
- ❖ Benchmarking of management remuneration in itself is challenge.
- ❖ There are no uncontrolled comparable transactions are available owing to the fact that management remuneration in all cases is a related party transaction.
- ❖ Salary of directors is determined by the management based on several factors viz qualifications, experience which are individual traits and varies from company to company.
- ❖ Certain judicial precedents have accepted the view that if the managerial remuneration is within the limits prescribed in the Companies Act, 1956, the same is a reasonable expenditure under section 40A(2)(b).

Benchmarking of Managerial Remuneration



| S no | Comparable | Analysis |
|------|--|--|
| 1 | Limits prescribed under the Companies Act, 1956 and/or central government approval | <ul style="list-style-type: none">• Taxpayers could rely on judicial precedents⁴ which have held the following:<ul style="list-style-type: none">– Quantum of remuneration is a business decision, influenced by business considerations and differs across companies.– Remuneration paid in accordance with the Companies Act, 1956 should not attract disallowance.• The above should be supported by the remuneration policy of the company. |
| 2 | Benchmarking from external agency | <ul style="list-style-type: none">• Determining the cost involved in recruitment of another personnel with similar qualifications, experience levels, skill sets and operational capabilities. |

Indirect Shareholding : Covered?



Direct v indirect ownership

Whether 'beneficial ownership' includes direct as well as indirect shareholdings is debatable. Judicial precedents² have held that the beneficial owner is the immediate shareholder.



Further, the revised ICAI Guidance Note (August 2013) on transfer pricing suggests that it may be appropriate to consider only direct shareholding and not indirect or derivative shareholding, and emphasises the real owner of the shares rather than the nominal owner.



The taxpayer needs to undertake a detailed analysis of its beneficial ownership to determine coverage.



TAX HOLIDAYS UNDERTAKINGS



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Following undertaking are covered

| Particulars | Coverage |
|---|---|
| Undertaking claiming industry based Tax Holidays | Undertaking engaged in generation/transmission/distribution of power or developing/operating/maintaining infrastructure facilities Companies engaged in refining, Oil, undertakings engaged in developing and building housing projects etc. |
| Undertaking claiming geographical location based tax holidays | Undertaking located in SEZ Undertaking located in Backward Industrial area Undertaking located in north Eastern States etc. |





Section 80A(6) and 80IA(8)

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Section 80A(6) and 80IA(8)

- ❖ Covers intra division transfer of Goods and Services
- ❖ Influences a case where taxpayer is entitled to deduction u/s. 10A or s.10AA or s.10B or s.10BA or Chapter VI-A in respect of undertaking or unit or Enterprise, where:
 - > Goods or services held for the purpose of eligible business are transferred to “any other business”,
 - > Goods or services held for the purpose of “any other business” transferred to eligible business,
 - > Consideration recorded in books does not correspond to market value of such goods
- ❖ Inter unit transfer between two non-eligible units has no TP implications.
- ❖ Section requires “any other business” carried on by assessee and dealings between businesses
- ❖ Restricted to goods and services of ‘marketable’ nature
- ❖ Restricted to transfer



Section 80A(6) and 80IA(8)

Activities which are not carried on as business

- ❖ HO expenses including IT support, accounts, law compliance etc
- ❖ Use of corporate resources, including IPR
- ❖ HO finance out of capital or accumulated profits
- ❖ Temporary use of funds

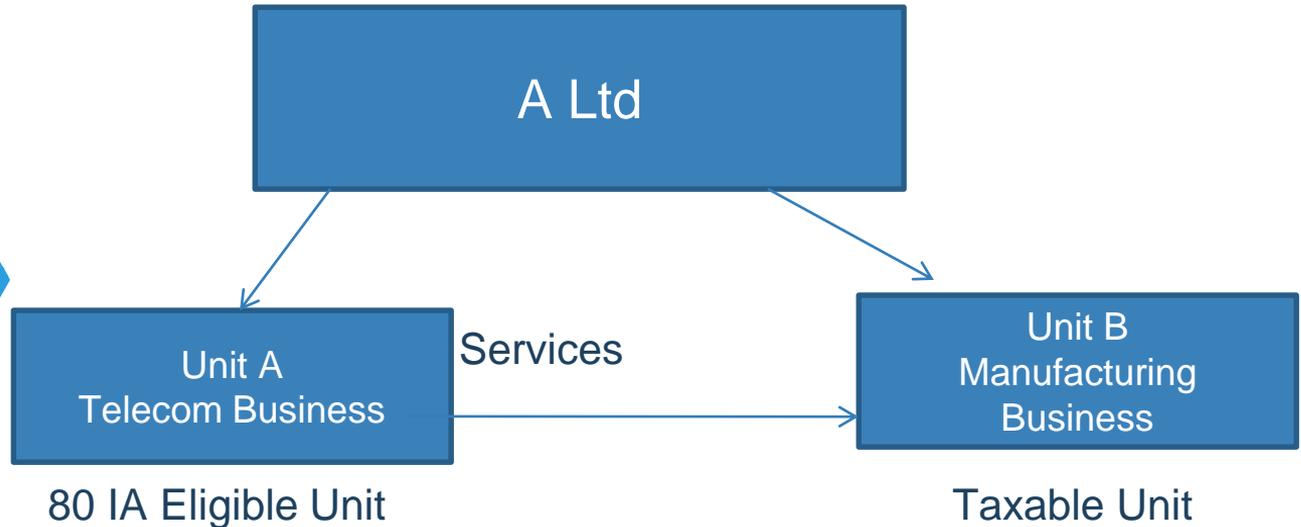
Allocation of actual expenses and challenges around allocation keys

- Research cost, finance cost, HO overheads, sales promotion

Provides for a “two-way” adjustment (both favorable as well as adverse)

If SDT, adjustment w.r.t. ALP; if not SDT, adjustment w.r.t. FMV

TRANSACTIONS COVERED



Transfer at Rs 120

Market Value of above goods/ services is Rs 100

Thus, the ALP of the above transaction would be Rs 100

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Section 80IA(10)

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Section 80IA(10)

Needs to be a “transaction” with “other person”

Ingredients which trigger invocation of s. 80-IA(10)

- ❖ Assessee carrying on eligible (tax holiday) business
- ❖ If it appears to AO
- ❖ Owing to **close connection** or otherwise
- ❖ Course of business arranged
- ❖ Transaction produces more than ordinary profit in tax holiday unit

- ❑ No need to report transaction unless conditions for invocation established
- ❑ Scope not restricted to goods or services
- ❑ Scope not restricted to S.40A(2) persons

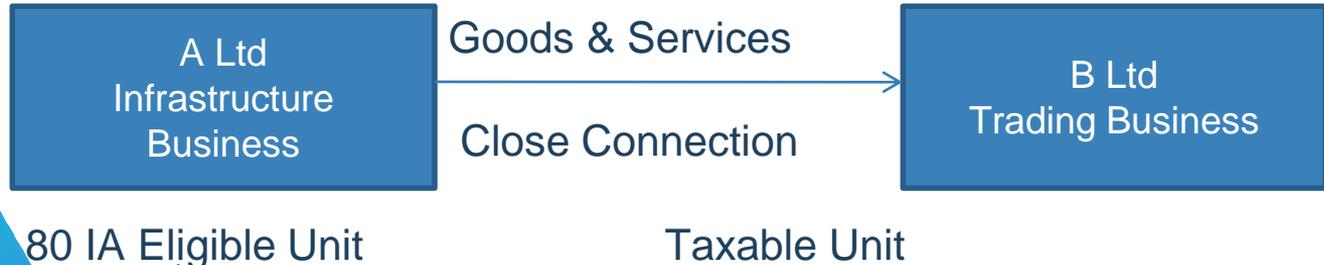
- ❑ Revenue >ALP does not per se imply existence of more than ordinary profits.
- ❑ If conditions fulfilled
- ❑ Transaction qualifies as SDT → adopt ALP,
- ❑ Transaction not SDT → AO to impute reasonable profits

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TRANSACTIONS COVERED UNDER SECTION 80IA(10)



Operating Margin: 40% (Extraordinary Profits)
Industry Average: 10%
Thus, Arm's length profit margin would be taken as 10%

80IA(8) & (10) – ISSUES AND CHALLENGES

- Issues in claiming corresponding credit when both units are eligible for tax holiday
- The term “Close Connection” not defined and subject to litigation
- Whether the term “more than ordinary profit” can be equated with ALP?
- Whether Capital account transactions are covered?



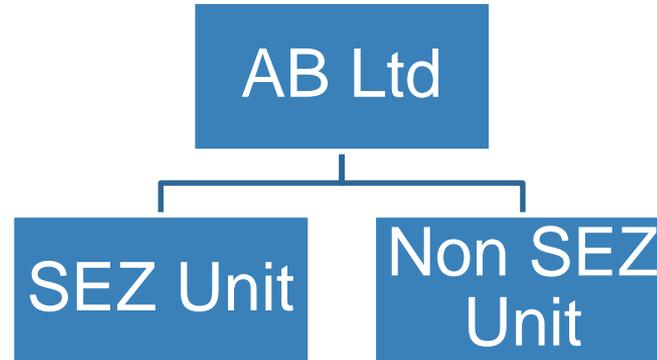
Illustrations

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Eligible business – Illustration 1



Facts

- ▶ AB Ltd is an IT Services Co. which commenced its operations in a non-SEZ unit. In addition to providing IT services, the unit also has the key management & marketing people and undertakes key value adding functions for the company as a whole.
- ▶ AB Ltd has recently set up a new SEZ unit . The unit is engaged in providing IT services to new customers. The unit houses the key delivery / project managers. The unit relies on certain knowledge tools/ technologies developed by the non-SEZ unit. Contracts are obtained/ signed by the management located in non-SEZ unit.
- ▶ AB Ltd allocates all revenues from the new contracts to the SEZ unit. Commons costs are allocated between the units based on a reasonable allocation key.



Eligible business – Illustration 1



Issue

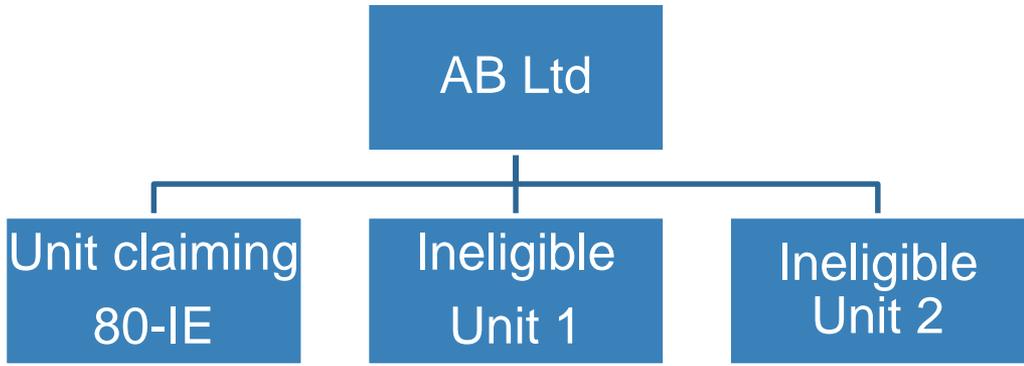
Assessing impact of SDT TP provisions on the profits of the SEZ unit

Approach

- ▶ Determine whether the SEZ unit and non-SEZ unit businesses should be regarded as separate businesses
- ▶ Evaluate whether there is transfer of goods/ services by non-SEZ unit to SEZ unit
- ▶ Evaluate whether common cost allocation is required under general principles or under SDT provisions and manner in which allocation is to be made
- ▶ Undertake functional analysis to determine appropriate characterization of the relationship between SEZ unit and non-SEZ unit
- ▶ Undertake economic analysis to determine appropriate arm's length approach for pricing the transactions
- ▶ Consider opportunities to optimize tax holiday benefits
- ▶ Consider approach to compliance/ disclosure



Eligible business – Illustration 2



Facts

- ▶ AB Ltd has three units. One in a North Estate state and availing benefits u/s 80-IE and two other units not availing any income linked deduction and is maintaining separate accounts
- ▶ AB Ltd has taken an interest bearing loan for setting up the 80-IE unit and unit 1. However, interest cost is not allocated to the units
- ▶ Funds lying in the separate accounts of the non-eligible units have been used to settle expenses of the eligible units. These reflect as receivable or payable in the separate accounts and get ultimately adjusted on consolidation



Eligible business – Illustration 2



Issue

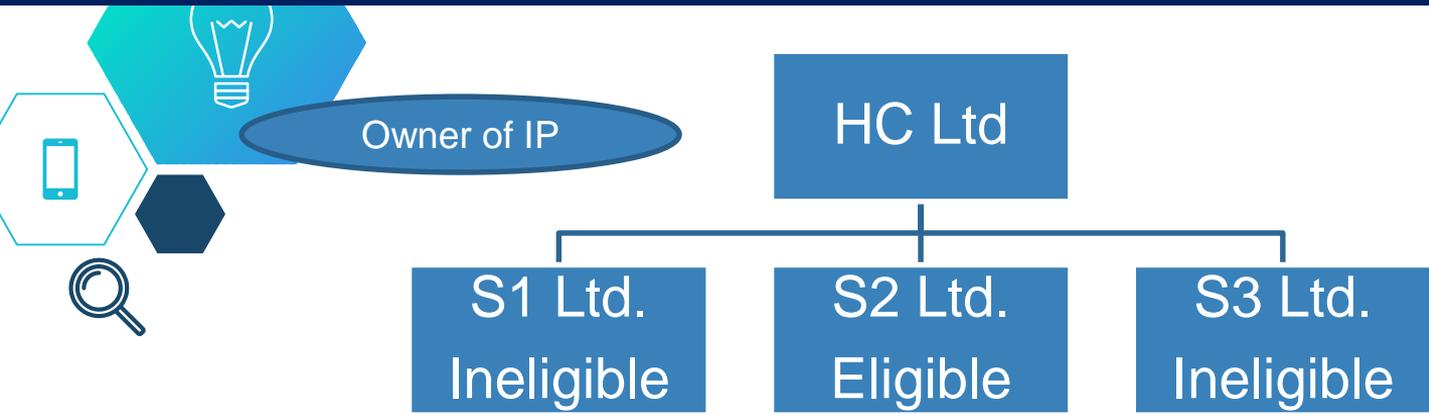
▶ Assessing impact of SDT TP provisions for determining profits of 80-IE unit – specifically whether the profits can be downward adjusted by allocating arm’s length interest for the loan/ use of funds

Approach

- ▶ Evaluate whether allocation of interest to 80-IE unit required under general principles for determining tax holiday or in view of SDT provisions and the manner in which the allocation is to be made.
- ▶ Determine whether the transaction relating to inter unit temporary use of funds could be regarded as provision of services by ineligible business to an eligible business
- ▶ If so, evaluate the approach for determining arm’s length charge for the service
- ▶ Consider approach to compliance/ documentation



Eligible business/Section 40A(2) – Illustration 3



Facts

- ▶ HC Ltd has three subsidiaries. One of the subsidiaries, S2 Ltd. is availing tax holiday under Chapter VI-A
- ▶ HC Ltd owns knowhow/ trademarks and it has licensed it to all the three subsidiaries. A uniform royalty rate of 1% on sales is charged. However, no royalty is charged if a subsidiary does not earn a pre-royalty targeted profit.
- ▶ During a particular financial year, S2 Ltd. and S3 Ltd were not charged royalty as they did not achieve the targeted profit level. A 1% royalty was charged to S1 Ltd



Eligible business/Section 40A(2) – Illustration 3



Issue

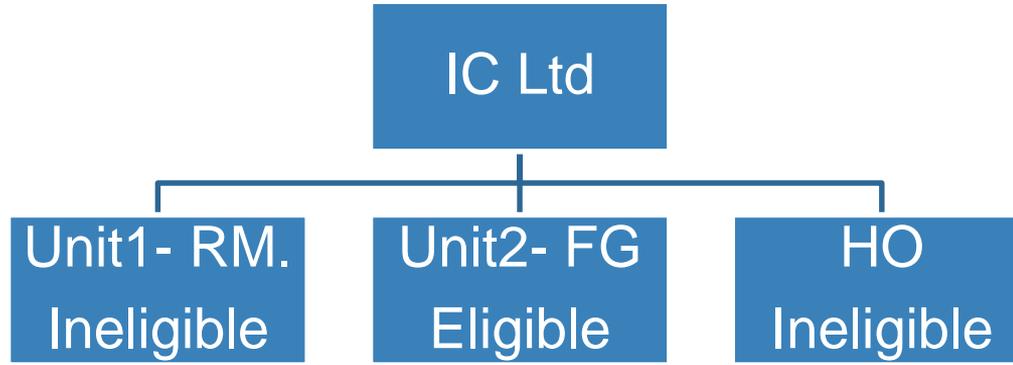
- ▶ Assessing impact of SDT TP provisions to the described fact pattern

Approach

- ▶ Undertake bench-marking exercise to identify comparable uncontrolled royalty transactions. In the absence of such data, evaluate application of other methods for establishing arm's length royalty rate
- ▶ Evaluate whether not charging arm's length royalty to S2 could be subjected to provisions of 80-IA(10) and assess whether economic analysis could support not charging royalty having regard to facts and circumstances.
- ▶ Consider approach to compliance/ documentation



Eligible business – Illustration 4



Facts

- ▶ IC Ltd. is an Indian automobile company having two units . Unit 2 is eligible for deduction under Chapter VIA,
- ▶ Unit 1 is engaged in manufacture of auto components. Unit 2 is engaged in assembly using the components manufactured by unit 1. IC Ltd. administers /monitors the operations of the company from its HO
- ▶ All key functions relating to purchase/manufacture are undertaken by Unit 1, strategic and marketing functions are performed by personnel in the HO. Unit 2 is engaged in routine assembly & delivery function
- ▶ In addition, HO also provides internal admin support such as payroll, accounting, general management, etc to both the units



Eligible business – Illustration 4



Issue

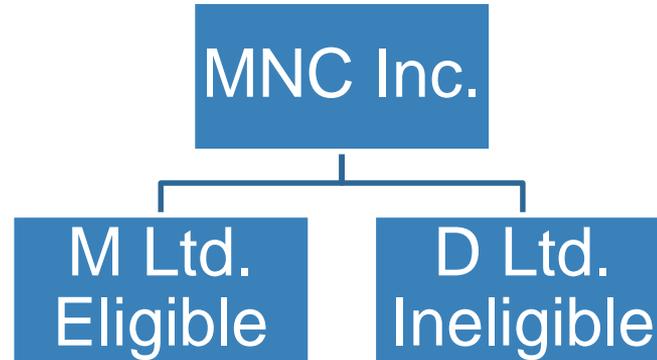
- ▶ Assessing impact of SDT TP provisions to the described fact pattern

Approach

- ▶ Evaluate whether allocation of HO costs required under general principles for determining tax holiday or in view of SDT provisions and the manner in which the allocation is to be made.
- ▶ Undertaking functional analysis to allocate functions/ assets/ risks between unit 1 and unit 2 and whether HO should be treated as a separate business for purpose of SDT
- ▶ Determine appropriate characterization of units for application of arm's length principle for inter-unit transfer of goods.
- ▶ Undertake a search for comparable data for determining pricing for inter-unit transfer
- ▶ Consider opportunities to optimize tax holiday eligibility
- ▶ Consider approach to compliance/ documentation



Eligible business and Section 40A(2) – Illustration 5



Facts

- ▶ MNC Inc., a foreign company has two subsidiaries in India i.e. M Ltd. and D Ltd.
- ▶ M Ltd. is engaged in manufacturing of goods and is eligible for tax holiday under Ch VI-A. D Ltd. is engaged in marketing and distribution of goods manufactured by M Ltd. to customers in India



Eligible business and Section 40A(2) – Illustration 5



Issue

▶ Assessing impact of SDT TP provisions to the described fact pattern – application of 80-IA(10) to inter-company sale to D Ltd and application of 40A(2) to purchase by D Ltd



Approach

▶ Undertake functional analysis to determine the appropriate characterization of the entities/ transactions

▶ Evaluate whether arm's length testing at one of the entities could be relied upon for establishing arm's length price for sale by M Ltd and purchase by D Ltd and if so testing for which of the entities is more appropriate.

▶ Determine application of most appropriate TP method to test arm's length pricing

▶ If necessary, evaluate and document the factors which justify the profits earned by M Ltd demonstrate that the same is not on account of an arrangement between M Ltd and D Ltd

▶ Consider opportunities to optimize tax holiday eligibility

▶ Consider approach to compliance/ documentation



80IA(8) & (10) – ISSUES AND CHALLENGES



Section 80-IA(8) covers business transactions undertaken by a taxpayer claiming tax holiday with other entities having ‘close connection’ with the taxpayer.

The Term ‘close connection’ has not been expressly defined in the Act.

For this reference could be drawn from other provisions of the Act to define ‘close connection’ as under:

“Substantial interest’ as defined under section 40A(2)(b);

“Associated Enterprises’ as defined under section 92A(2); and

“Related party’ defined as per Accounting Standard – 18 issued by ICAI

Close Connection



| Particulars | Substantial interest - section 40A(2)(b) | Associated enterprise - section 92A(2) | Related party as per AS – 18 as issued by ICAI |
|------------------------------------|--|--|---|
| Voting power | $\geq 20\%$ | $\geq 26\%$ | $>50\%$ |
| Direct or indirect holding covered | No* | Both | Both |
| Directors covered | Covered | Covered | Key managerial personnel covered |
| Key suppliers covered | Not covered | Supplying more than 90% | Specifically excluded |

80IA(8) & (10) – ISSUES AND CHALLENGES

- Section 80-IA (10): Where the Revenue authorities believe that the tax holiday undertaking produces more than ordinary profits due to a close connection with any person, only a reasonable level of profits will be eligible for the tax holiday benefit.
- For domestic transfer pricing, ordinary profits for tax holiday units would need to be determined having regard to the arm's length principle and the transfer pricing methods.
- If price based method (say, the Comparable Uncontrolled Price method) has been applied to benchmark the transaction between and a person closely connected with it, the derived profits may be considered as ordinary profits, in view of absence of horizon of the comparables margin.

80IA(8) & (10) – ISSUES AND CHALLENGES



Issue

Approach

Whether allocation of costs is a SDT

- Relying on judicial precedent⁵, taxpayers may argue that pure cost allocations to determine appropriate profits of the undertaking do not entail a service and accordingly, are not covered under DTP provisions.

Determination of allocable costs

- An ideal cost allocation policy would entail allocation of 'all' common costs based on rational allocation keys.

Determining reasonable allocation keys

- Expenses ought to be allocated on a reasonable and scientific basis (say, on the basis of ratio of turnover, head-count, cost of sales, etc.).

Allocation of costs – whether at actual or at mark-up

- Where the services are of a marketable nature, the relevant costs could be charged at a mark-up and reported in Form 3CEB.



CONSEQUENCES OF TP ADJUSTMENT



CONSEQUENCES OF TP ADJUSTMENT



- S.40A(2)(b) disallowance leads to enhancement of income and consequential tax /interest levy
- No consequential enhancement of s.10AA/Chapter VI-A deduction. (First proviso to s.92C(4))
- S.80A(6) /s.80-IA(8) /s.80-IA(10) adjustment leads to curtailment of tax holiday deduction leading to additional income and consequential tax, interest levy
- No co-relative adjustment in the hands of the recipient
- Penal consequences



DOMESTIC TRANSFER PRICING CASE LAWS ON DTP PRIOR TO INTRODUCTION OF DETAILED DTP REGULATIONS



IN THE CONTEXT OF SECTION 40A(2)

- **KR Motilal v. CIT (1999) (240 ITR 810) (Mad)**

- The assessee engaged in the business of manufacture of three wheel cycles
- Payment of remuneration and commission to brothers of the assessee for providing technical and supervisory services
- The AO disallowed the same u/s 40A(2)



IN THE CONTEXT OF SECTION 40A(2)

– ITAT held that:

Part of the remuneration / commission paid to brothers is excessive and unreasonable and thus to be disallowed u/s 40A(2) since:

The assessee was unable to justify possession of technical qualifications / technical skill by the brothers required to handle the job

Unable to produce supporting to substantiate the technical experience of brothers



IN THE CONTEXT OF SECTION 40A(2)

- **Mangal Chand Tubes Pvt. Ltd. v. CIT (1994) 208 ITR 729 (Raj)**
 - Payments to two directors for managing the operations for the same area
 - The AO disallowed part of the payments made to one of the director u/s 40A(2)
 - Rajasthan High Court upheld the AO's order and held that:
The disallowance made by the AO is justified since one of the directors who was permanently stationed in the same region (Delhi) was looking after the day to day functions of the company and business needs of the company did not warrant payments to another director.

A decorative graphic on the left side of the slide consists of several hexagons in shades of blue and teal. Some hexagons contain icons: a lightbulb, a thumbs-up, a smartphone, a magnifying glass, and a gear. There is also a network of nodes and lines, and a speech bubble icon. The text 'IN THE CONTEXT OF SECTION 40A(2)' is written in a large, teal, sans-serif font across the top of the graphic area.

IN THE CONTEXT OF SECTION 40A(2)

The assessee was unable to justify commercial rationale of making payments to both directors and how it benefited its operations

Legitimate business needs of the company did not warrant incurrence of such expenditure

A decorative graphic on the left side of the slide consists of several hexagons in shades of blue and teal. Some hexagons contain icons: a lightbulb, a thumbs-up, a smartphone, a magnifying glass, and a gear. There is also a network of nodes and lines, and a speech bubble. The text 'IN THE CONTEXT OF SECTION 40A(2)' is written in a light blue, sans-serif font across the top of the graphic area.

IN THE CONTEXT OF SECTION 40A(2)

Whether HO expenses are required to be allocated among units?
ACIT v. Asea Brown Boveri Ltd. (2007) 110 TTJ 502 (Mum)

It was held that HO expenses are required to be allocated since HO is a cost centre which is common to all the units. It does not exist for its own sake but its existence is relevant for all the activities undertaken by various divisions, units and profit centre

Similarly, in the following cases, it was held that HO expenses are required to be allocated based on rationale allocation keys:

CIT v. S T Micro Electronics Pvt. Ltd. (2011-TIOL-499-HC-DEL-IT)

Wipro GE Medical Systems Ltd v. DCIT (2003) 81 TTJ 455 (Bang)



IN THE CONTEXT OF SECTION 80IA(10)

M/s Tweezerman India Pvt Ltd Vs. Addl. CIT (2010-TII-45-ITAT-MAD-TP)

The assessee (Indian Company) engaged in manufacturing of tweezers and eligible for 10B deduction exported 100% to its US AE

- TPO accepted the value of ITs at ALP and passed remark that Arm's length profit would be Rs. 733.42 lacs as against Rs. 1,251 lacs reported by the assessee
- AO invoked Section 10B(7) r.w.s.80IA(10) and reduced 10B deduction
- ITAT deleted the addition and held that:
Section 80IA(10) does not give an arbitrary power to the AO and the AO has to specify as to why he feels that the profits of the assessee is shown at a higher figure.

A decorative graphic on the left side of the slide consists of several hexagons of various colors (teal, blue, dark blue) and icons. The icons include a lightbulb, a thumbs-up, a network of nodes, a smartphone, a magnifying glass, a gear, and a speech bubble. A large teal-to-blue gradient hexagon is positioned in the center of this graphic.

IN THE CONTEXT OF SECTION 80IA(10)

Further, AO has to show as to how he has computed the ordinary profits which the assessee might be expected to generate

AO has blindly taken a calculation for determining the ordinary profits which the assessee had given before the TPO and admitted it to be erroneous



DOMESTIC TRANSFER PRICING COMPLIANCES



COMPLIANCE REQUIREMENTS FOR DOMESTIC TRANSFER PRICING

Current Compliance Requirements

Section 40A: Transactions to be reported in Tax Audit Report in Form 3CD

Section 80IA: Declaration of profit to be made in CA Certificate in Form 10CCB

Section 10AA: For claiming tax deduction, CA Certificate in Form 56F needs to be filed

COMPLIANCE REQUIREMENTS FOR DOMESTIC TRANSFER PRICING

Additional Compliance Requirements

Maintaining Contemporaneous Documentation as prescribed in Rule 10D and prove that transactions are at ALP by selecting the most appropriate method

Filing audit report in Form 3CEB / any other Form may be prescribed

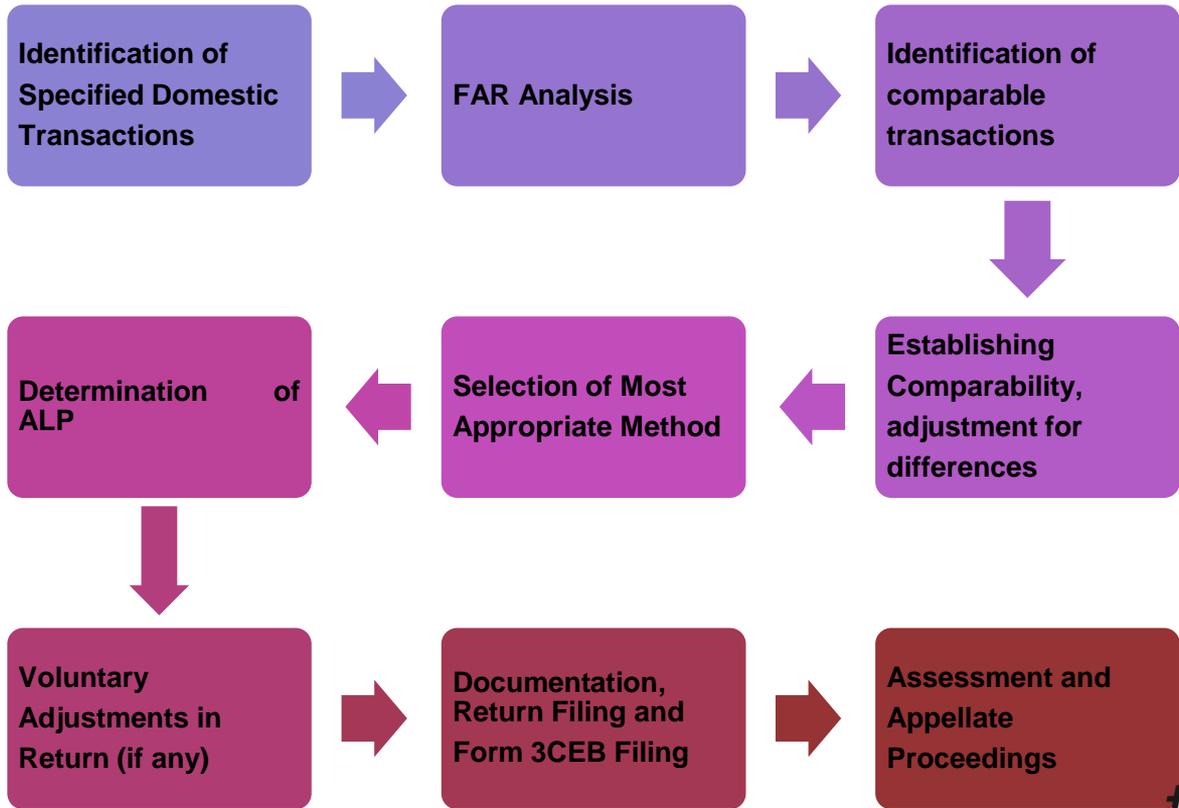
COMPLIANCE REQUIREMENTS FOR DOMESTIC TRANSFER PRICING

Then and Now position

- ◇ **Then**, it was mere reporting of transactions in Form 3CD and Form 10CCB,
- ◇ **Now**, reporting of justification of a price charged along with arm's length price in Form 3CEB (*Part C of Form 3CEB*)
- ◇ • **Then**, generic justification or comparison was still sufficient,
- ◇ - **Now**, scientific justification based on prescribed methods is to be maintained
- ◇ • **Then**, normal documentary evidences were sufficient,
- ◇ - **Now**, TP documentation supported by robust supportings required
- ◇ • **Then**, related party transactions used to be scrutinized at the assessment stage by the Assessing Officer,
- ◇ - **Now**, the assessee is duty bound to maintain justification and file mandatory
- ◇ Chartered Accountant's report at the threshold
- ◇ • **Then**, related party transactions not so closely scrutinized by the AO,
- ◇ - **Now**, there will be aggressive monitoring by the TPO/AO



DOMESTIC TRANSFER PRICING – PROCESS FLOW



VARIOUS METHODS FOR DOMESTIC TRANSFER PRICING



| Method | Applicability | PLI to be used |
|---|---|--|
| CUP | CUP method can be applied where reliable data of similar uncontrolled transaction between two unrelated parties or between related party and third party is available | Prices |
| RPM | Where an enterprise purchases goods or services from a related party and sells them to unrelated parties without adding any substantial value to the product or services | Gross Profit Margin |
| CPM | Where there is transfer of semi finished goods between related parties or in case of services | Gross Profit Margins/ Direct & Indirect Cost of Production / service |
| PSM | In case of transfer of unique intangibles or in multiple inter-related transactions which cannot be evaluated separately for determining the arm's length price | Generally, operating Profit Margins |
| TNMM | When all other methods for determining ALP fails and reliable comparable data with broad functional similarity is available | Generally, operating Profit Margins |
| Other method to be used as per Rule 10 AB | Where the price which would be charged for similar transaction between unrelated parties is available (based on the valuation reports, genuine quotes available from Independent parties, etc.) | Such "would be Price" |



Key challenges and issues in determining ALP

- ❖ Difficulty in benchmarking certain unique transactions for which comparability data may be difficult to obtain. For eg. Directors remuneration
- ❖ Comparability standards for bench marking profits/margins of eligible business
 - ✓ For evaluating ALP for Section 80A(6)/80IA(8)/80IA (10) transactions, should comparability be with enterprises that do not enjoy tax holiday?
 - ✓ Alternatively, determine ALP return for” non eligible business” and allocate residual to “ eligible business”
 - ✓ Availability of adequate data/information in public domain
- ❖ Identification/ demarcation of eligible business and non eligible business for determining existence of “ 80A(6)/80A(8) transactions”
- ❖ Identifying parties with whom taxpayers have “ close connection” and assessing reasons for more than arms length profits, if any





INFORMATION & DOCUMENTATION REQUIREMENTS



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INFORMATION & DOCUMENTATION REQUIREMENTS

Entity Related

Group Profile
(incl. Organization structure)

Indian Entity Profile
(incl. description of transactions)

Related Party Profile

(incl. description of transactions)
Industry Profile

Price Related

Transaction Terms
Functional, Asset and

Risk ('FAR') Analysis
Economic Analysis

(selection of the most appropriate method, benchmarking and determining ALP)

Transaction Related

Agreements

Invoices

Pricing related correspondence
(letters, emails, etc)

Internal presentation & business plan

Brochures & Catalogues

Management's accounts & reports

COMMON TRANSACTIONS DOCUMENTATION



| Transaction entered | Documents to be maintained | |
|--------------------------------|--|--|
| Purchase/ sale of raw material | <ul style="list-style-type: none">- Invoices- Purchase/ Sale order- Product details- Sale details if sold to 3rd Party | <ul style="list-style-type: none">- Pricing strategy- Proof of price negotiation- Quotes from competitors- Terms of payment |
| Remuneration to Directors | <ul style="list-style-type: none">- Qualification- Work Experience & Profile- Minutes of Meeting authorizing the director's remuneration | <ul style="list-style-type: none">- Data from HR firms for Directors in the same line of business |
| Corporate cost sharing | <ul style="list-style-type: none">- Nature of expenses- Auditor's certificate allocating the expenses | <ul style="list-style-type: none">- Basis of allocation between the companies- Proof of usage (rendering) of services- Cost benefit analysis |

COMMON TRANSACTIONS DOCUMENTATION



Transaction entered

Documents to be maintained

Rent paid toward use of premises

- Rent receipts
- Documents suggesting the rent of the surrounding area

- Rental agreement
- Fair market value of the property (municipal valuation, only if higher than the actual rent paid)

Reimbursement of expenses

- Nature of expenses with detailed break-up
- Reason of expense incurred for

- Employee details
- Actual invoices of the expense

Interest on loan (nonfinancial services company)

- Basis of determination of interest rate
- Interest Rate Card for the period of loan

- Loan agreement
- Basis on which the interest rate is pegged above standard rate



TRANSFER PRICING COMPLIANCES & PENALTIES ON DEFAULT



TRANSFER PRICING COMPLIANCES & PENALTIES



| Particulars | Compliances to be followed | Penalty, if not complied with |
|--|--|---|
| Filing of the Audit Report in Form 3CEB | Mandatory to file Form 3CEB before the due date of filing return of income if the value of SDT exceeds INR 5 crs or even if there is international transaction with Associated Enterprise of even a single Rupee | Rs 1,00,000 [Section 271BA] |
| Reporting of each SDT and international transaction entered into with related party in Form 3CEB | Mandatory to report every transaction in Form 3CEB | 2% of the value of each transaction not reported [Section 271AA] |
| Maintenance of Transfer Pricing Documentation | Mandatory to maintain robust documentation where transactions subject to Transfer Pricing exceed 1 cr. in a financial year for international transaction & INR 5 cr for SDT | 2% of the value of each transaction [Section 271AA] |

TRANSFER PRICING COMPLIANCES & PENALTIES



| Particulars | Compliances to be followed | Penalty, if not complied with |
|---|--|--|
| Maintenance and furnishing of correct information / documents before AO and CIT(A) | Mandatory to maintain and furnish correct information / documents before AO and CIT(A) | 2% of the value of each transaction for false reporting [Section 271AA] |
| Concealment of particulars of income and furnishing inaccurate particulars thereof. | Mandatory to furnish correct particulars of transactions before the Revenue authorities | Penalty ranging from 100% to 300% of the amount of tax sought to be evaded if adjustment is made by the Revenue authorities [Explanation 7 to Section 271(1)(c)] |
| Failure to furnish information or documents as required under section 92D(3) | Mandatory to furnish information or documentation required by the Revenue authorities within timelines as per section 92D(3) | Penalty @ 2% of the value of the transaction for each such failure [Section 271G] |



FORM 3CEB



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Accountants Report

- Prepared by every person/enterprise entering into an international transaction or SDT with AE/related party
- To be filed by the due date for filing return of income
- Opinion as to whether prescribed documents have been maintained and the particulars in the report are “true and correct”
- An important document for the Assessing Officer**
- Contains summary of international transactions / SDTs
- Contains details of taxpayer
- Contains methods employed to determine ALP
- Date of e filing of Form No.3CEB is required to be mentioned in the Return of Income
- Digital Signature, Name, Membership number, Date, Firm Name and Registration number

Form No. 3CEB
[See rule 10E]

Report from an accountant to be furnished under section 92E relating to international transaction(s) or specified domestic transaction(s)

1. We have examined the accounts and records of <<name of the entity>>, with its registered office at <<insert address>> having Permanent Account Number <<XXX>> that have been made available to us relating to the international transaction(s) or specified domestic transaction(s) entered into by the assessee during the previous year ending on 31 March 2014.
2. In our opinion proper information and documents as are prescribed have been kept by the assessee in respect of the international transaction(s) or specified domestic transaction(s) entered into so far as appears from our examination of the records of the assessee.
3. The particulars required to be furnished under section 92E are given in the Annexure to this Form. In our opinion and to the best of our information and according to the explanations given to us, the particulars given in the Annexure, as read with notes appended thereto, are true and correct.

Place : _____

Date : _____

For XXXX

Chartered Accountants
Membership Number



Features of Form 3CEB

Para 1

****I/we have examined the accounts and records of (name and address of the assessee with PAN) relating to the international transactions and specified domestic transactions entered into by the assessee during the previous year ending on 31st March,***

1. Cases where books/ accounts of foreign companies are not available ?
2. Reliance on the statutory audited results in case you are not the statutory auditor.

“For the purpose of this report we have relied upon the accounts of the assessee for the year ended 31 March 2014 audited by <<insert name of the auditors>> vide their audit report dated <<insert date>>.”

3. Reliance on management prepared accounts in case of different statutory year end.



Features of Form 3CEB

Para 2

In *my/our opinion proper information and documents as are prescribed have been kept by the assessee in respect of the international transactions and the specified domestic transactions entered into so far as appears from *my/our examination of the records of the assessee”.

1. Auditor signing the Form 3ceb, needs to check whether proper documentation maintained
2. Documentation requirement prescribed in Sec 92 D read with Rule 10 D
3. Exemption from preparing detailed documentation, if the international transaction value less than INR 1 crores -However, the Assessee must maintain documents to justify ALP.
4. More onus on auditor to satisfy whether adequate / appropriate documentation maintained --If any required document is not maintained, the Accountant should qualify the report or disclose the same.
5. Reporting and Documentation, if SDT exceeds INR 5 crores





Features of Form 3CEB



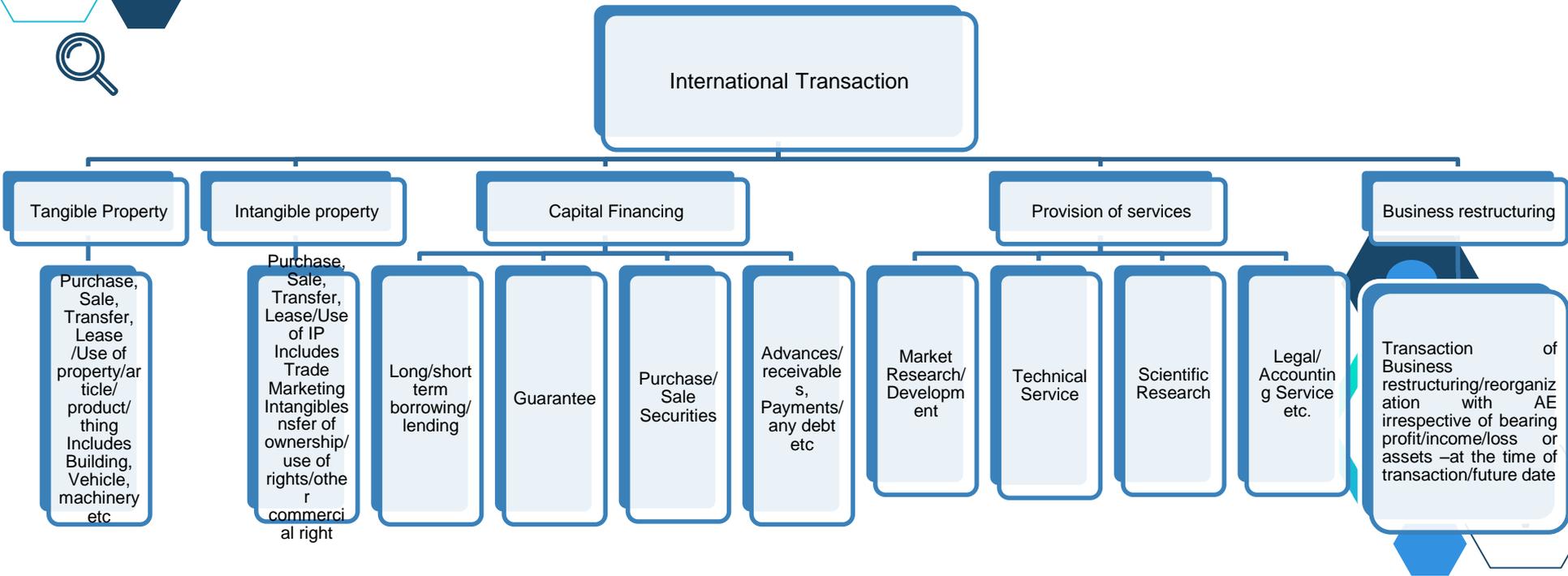
Para 3

The particulars required to be furnished under section 92E are given in the Annexure to this Form. In *my/our opinion and to the best of my/our information and according to the explanations given to *me/us, the particulars given in the Annexure are true and correct”

- 1. True and correct v/s True and fair -Emphasis on factual accuracies.*
- 2. Foreign companies –disclose the incapacity to gather all information*
- 3. Limit the scope of work and review procedures to extent certified by him in Form 3CEB*
- 4. Most appropriate method -Para 9.17 of the revised GN*



International Transaction –Section 92B





Specified Domestic Transactions –Section 92BA



Specified domestic transactions

Any expenditure in respect of which payment has been made or is to be made to a person referred in clause (b) of subsection 2 of 40A

Any transaction referred to in section 80A

Any transfer of goods or services referred to in subsection (8) of section 80-IA

Any business transacted between assessee and other person as referred to in subsection (10) of section 80-IA

Any transaction referred to in any other section under Chapter VIA or section 10AA to which subsection (8) or (10) of section 80-IA applies

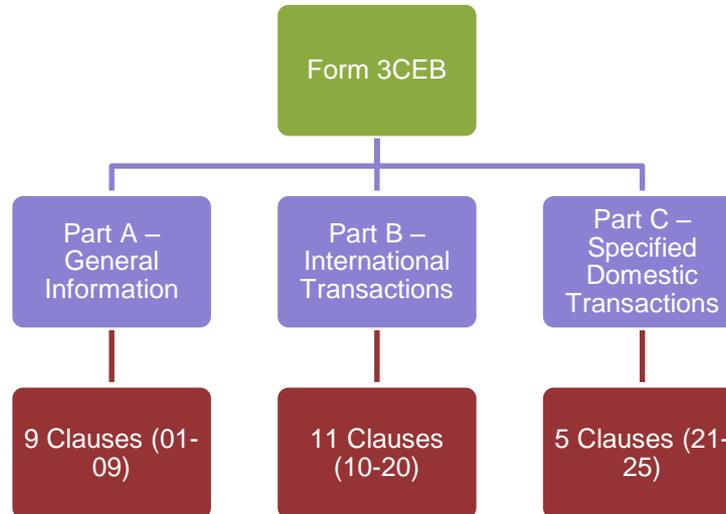
Any other transaction as may be prescribed



The New Form 3CEB

Vide the Notification, the Government has notified the new Form 3CEB, as part of Appendix-II of the Primary Rules.

The 3CEB, erstwhile with 13 clauses for internal transactions has now been replaced with a new form, with 25 clauses:





Annexure to Form No. 3CEB –A Glimpse



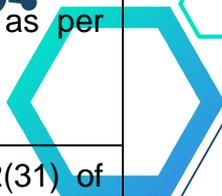
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Annexure to Form No. 3CEB



| Clauses | Description |
|--|--|
| Clause 1: Name of assessee | Full and complete name In case of change in name, write both new and old name |
| Clause 2: Address | In case of foreign company, provide foreign address |
| Clause 3: PAN | Permanent Account Number |
| Clause 4: Nature of business or activities of the assessee | Code for nature of business to be filled in as per instructions for filing Form ITR6 |
| Clause 5: Status | Refers to the person defined under Section 2(31) of the Act i.e. Company in our case |





Annexure to Form No. 3CEB



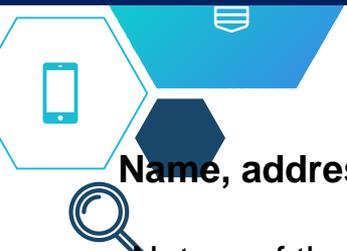
| Clauses | Description |
|--|--|
| Clause 6: Previous Year ended | 31March2014 |
| Clause 7: Assessment year | 2014-15 |
| Clause 8: Aggregate value of international transactions | Refers to value of transactions as per books of accounts |
| Clause 9: Aggregate value of specified domestic transactions | Refers to value of transactions as per books of accounts |

Clause 21: Illustration List of Related Parties with whom the assessee has entered into SDT with the necessary details

Clause 21 : List of associated enterprises with whom the assessee has entered into specified domestic transactions

| Sr. No. | Name of the associated enterprise | Address of the associated enterprise | PAN of the associated enterprise | Nature of the relationship with the associated enterprise | Brief description of the business carried on by the said associated enterprise |
|---------|--|--------------------------------------|----------------------------------|---|--|
| | Clause 21 (a) | | | Clause 21 (b) | Clause 21 (c) |
| 2 | ABC India Medical Ltd (Pune SEZ Unit) | Address>>>> | PAN >>>> | PAN >>>> ABC India Pvt Ltd beneficially owns shares having voting powers of not less than 20% of ABC India Medical Ltd | Manufacturing of Pharmaceutical Products |

Clause 21: Illustration List of Related Parties with whom the assessee has entered into SDT with the necessary details



Name, address and PAN of the related party(s)

- Nature of the relationship with related party
- Brief description of the business carried on by the said related party
- Cover details of relationships with managerial personnel, holding/subsidiary company, inter-unit transactions and those with closely connected persons

Key check points:

- Correct legal name of the related party (to be verified from the website / annual report) along with PAN details, etc
- Nature of relationship -to be specific; reference to clause of 92BA , verification using shareholding pattern, investment schedule, etc
- Whether indirect shareholding relationships covered?



Clause 22: Illustration Particulars in respect of transactions in the nature of any expenditure

Clause 22 : Specified domestic transaction(s) being any expenditure in respect of which payment has been made or is to be made to any person referred to in section 40A(2)(b)

| Sr No. | Name of the person with whom the specified domestic transaction has been entered into | Description of the transaction along with quantitative details, if any | | Total amount paid or payable in the transaction | | Method used for determining the arm's length price[See section 92C(1)] |
|--------|---|--|----------|---|--|--|
| | | Description of the transaction | Quantity | (i) as per books of account | (ii) as computed by the assessee having regard to the arm's length price | |
| 1 | ABC India Support Limited | | | | | |

Clause 22: Illustration Particulars in respect of transactions in the nature of any expenditure

- 
- Expenditures made to persons covered under section 40A(2)(b)of the Act. Emphasis on direct/indirect holding.
 - Transactions where tax holiday/deduction is claimed in respect of capital expenditure
 - Managerial remuneration
 - Expenditure for which no deduction /part deduction has been claimed
 - Reimbursements to related parties

Key check points:

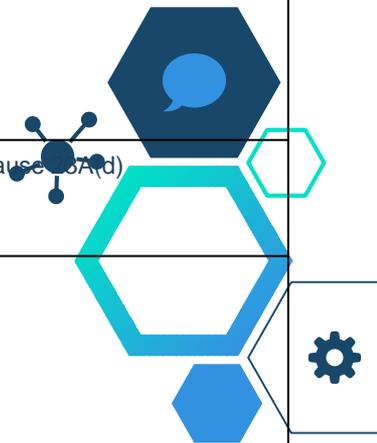
- Verify value and quantitative details from notes to accounts (in addition to AS 18), tax audit report, invoices and ledger accounts, fixed assets schedule, etc
- Service / employment contracts / agreements
- Minutes of board meetings for managerial remuneration
- Other relevant documents substantiating expenditure



Clause 23: Illustration Particulars in respect of transactions in the nature of transfer or acquisition of any goods or services

Clause 23A : Specified domestic transaction(s) in the nature of transfer or acquisition of any goods or services by an undertaking or unit or enterprise or eligible business of the assessee [as referred to in section 80A(6), 80IA(8) or section 10AA)] to any other business carried on by the assessee

| Sr. No. | Name and details of business to which goods or services have been transferred | | Description of goods or services transferred | Amount received / receivable for transferring of such goods or services | | Method used for determining the arm's length price[See section 92C(1)] |
|---------|---|----------------------------------|--|---|--|--|
| | Name of business | Details of business | | (i) as per books of account | (ii) as computed by the assessee having regard to the arm's length price | |
| | Clause 23A(a) | | Clause 23A(b) | Clause 23A(c) | | Clause 23A(d) |
| 1 | ABC India Support Ltd | Operating retail pharmacy stores | Purchase of Medicines | | | |



Clause 23: Illustration Particulars in respect of transactions in the nature of transfer or acquisition of any goods or services

Clause 23B: Specified domestic transaction(s) in the nature of transfer or acquisition of any goods or services by an undertaking or unit or enterprise or eligible business of the assessee [as referred to in section 80A(6), 80IA(8) or section 10AA] from another business of the assessee

| No. | Name and details of business to which goods or services have been acquired | | Description of goods or services acquired | Amount received / receivable for transferring of such goods or services | | Method used for determining the arm's length price[See section 92C(1)] |
|-----|--|----------------------------------|---|---|--|--|
| | Name of business | Details of business | | (i) as per books of account | (ii) as computed by the assessee having regard to the arm's length price | |
| | Clause 23B(a) | | Clause 23B(b) | Clause 23B(c) | | Clause 23B(d) |
| 1 | ABCIndia Medical Ltd –(Pune SEZ Unit) | Manufacturer of Medical Products | Sale of Medicines | | | |



Clause 23: Illustration Particulars in respect of transactions in the nature of transfer or acquisition of any goods or services

- 
- SDTs in nature of transfer/acquisition of any goods or services referred to in 80A(6),80IA(8)or10AA
 - Transactions for which tax holiday is not claimed by the Eligible Unit/Undertaking
 - Above covers income as well as expenditure transactions

Key check points:

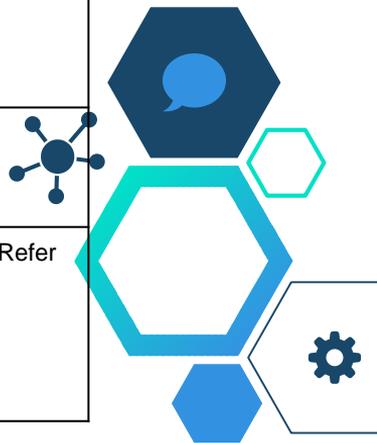
- Verify value and quantitative details from notes to accounts (in addition to AS 18), invoices and ledger accounts, fixed assets schedule, etc
- Review the agreement(s), invoices, debit notes raised
- Check for CUP i.e., whether services are provided to unrelated parties
- Profitability of the entity / division (related party / non-related party)
- Whether inter unit cost allocations are equivalent to 'expenditure' –whether same is required to be reported in this clause?



Clause 24: Illustration Particulars in respect of any SDT in the nature of business transacted

Clause 24 : Specified domestic transaction (s) in the nature of any business transacted which has resulted in more than ordinary profits to an eligible business to which section 80IA(10) or section 10AA applies

| Sr. No. | Name of the person with whom the specified domestic transaction has been entered into | Description of the transaction including quantitative details, if any | | Total amount received / receivable or paid / payable in the transaction | | Method used for determining the arm's length price[See section 92C(1)] |
|---------|---|---|----------|---|--|--|
| | | Description of the transaction | Quantity | (i) as per books of account | (ii) as computed by the assessee having regard to the arm's length price | |
| | Clause 24(a) | Clause 24(b) | | Clause 24(c) | | Clause 24(d) |
| 1 | ABC India Medical Limited | Sale of Equipment | 1 | 2,000,000 | 2,000,000 | Other Method (Refer to Note below) |



Clause 24: Illustration Particulars in respect of any SDT in the nature of business transacted

- 
- Transactions resulting in more than ordinary profits to an eligible business under section 80IA(10) or 10AA
 - Covers amounts paid/payable or received/receivable
 - TP study to be relied upon to determine whether transactions are at arm's length. Accordingly to be covered here only if transaction resulting in more than ordinary profit

Key check points:

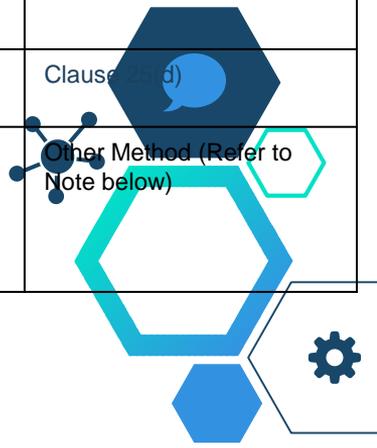
- Verify value and quantitative details from notes to accounts (in addition to AS 18), invoices and ledger accounts, fixed assets schedule, etc
- Review the agreement(s), invoices, debit notes raised
- Check for CUP i.e., whether services are provided to unrelated parties
- Profitability of the entity / division (related party and Non related party)



Clause 25: Illustration Particulars in respect of any other transactions

Clause 25 : Any other specified domestic transaction(s) not specifically referred to above in any other clauses, with an associated enterprise

| Sr. No. | Name of the person with whom the specified domestic transaction has been entered into | Description of the transaction | | Total amount received / receivable or paid / payable in the transaction | | Method used for determining the arm's length price [See section 92C(1)] |
|---------|---|--------------------------------|---|---|--|---|
| | | | | (i) as per books of account | (ii) as computed by the assessee having regard to the arm's length price | |
| | Clause 25(a) | Clause 25(b) | | Clause 25(c) | | Clause 25(d) |
| 1 | ABC India Medical Limited | Sale of Equipment | - | 2,000,000 | 2,000,000 | Other Method (Refer to Note below) |



Clause 25: Illustration Particulars in respect of any other transactions



Key check point:

- This residual clause is to cover transactions which may be prescribed per Section 92BA(vi). As there are no transactions which have been prescribed till date, this clause has to be replied by stating a “No”.





MRL is Management Representation in respect of Accountant's Report under section 92E of the Income Tax Act, 1961 relating to International /SDT Transactions of the assessee

MRL

Broad contents of MRL:

- Declaration as regards information / documents required as per Rule 10D are contained in TP Study Report.
- Declaration as regards to the completeness of international transactions and reconciliation with Audited Financial Statements
- Ownership Structure
- International transactions / SDT
- Most Appropriate Method followed
 - *if Cost Plus Method is used then details of costs included / not included while charging mark-up on costs is to be obtained from the client through MRL*

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RECENT DEVELOPMENTS



On 04 Feb 2015 CBDT notified safe harbour rules for SDT undertaken by Government Companies engaged in the business of generation, transmission or distribution of electricity. Tariff in respect of supply of electricity, transmission of electricity, wheeling in electricity as the may be determined by the appropriate commission will be accepted by the Tax authorities.

Range concept introduced

Use of Multiple year data allowed





Thanks for your valuable time

Stay connected

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